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State of Washington Joint Legislative Audit and Review Committee

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Linked Deposit Program Sunset Review Report 99-7

The Linked Deposit Program enables state-certified small businesses owned by minorities and women to obtain loans from participating private banks at reduced interest rates. The program does not have criteria for determining whether Linked Deposit loan applicants lack access to capital. Furthermore, it has weak controls and lacks performance measures. If the program is continued, the report recommends statutory and other modifications to improve these controls and measures.

Introduction

The Linked Deposit Program, created in 1993, is scheduled to terminate in June 2000. Its purpose is to increase access to capital for businesses owned by minorities and women (RCW 43.86A.060).

The Linked Deposit Program enables state-certified small businesses owned by minorities and women to obtain loans from participating private Washington banks at a reduced interest rate. The State Treasurer is authorized to use up to \$50 million of short-term state treasury surplus funds for this program.

Program funds are used for purchasing certificates of deposit equaling the amount loaned by private banks to certified businesses. The state earns two percentage points less in interest than the market rate on these certificates of deposit. This forgone interest is then passed on to borrowers, who pay two percentage points below the market rate on their loans. The certificates are not at risk of losing their value.

The Office of the State Treasurer, the Department of Community, Trade and Economic Development (CTED), and the Office of Minority and Women's Business

Enterprises (OMWBE) are involved in implementing the program.

The program has enabled 230 certified minority and women's business enterprises to obtain reduced interest rate loans. As of February 1999, a total of more than \$48 million of the \$50 million earmarked for the program was committed in certificates of deposit.

Compliance with Legislative Intent

The program has been implemented according to its authorizing legislation. However, criteria for determining the extent to which Linked Deposit loan applicants lack access to capital are absent in the legislation. Thus, it is difficult to assess whether the program has met the legislative intent to remedy the problem of a lack of access to capital for minority and women's business enterprises.

Furthermore, the program does not have a mechanism to prevent a few businesses from using a relatively large portion of program funds. This becomes important as the use of program funds reaches the \$50 million ceiling.

Economy, Efficiency, and Duplication

The program does not receive additional funds for its administration. The primary cost of the program is in forgone interest earnings—an estimated \$1.23 million per year—on \$50 million in state funds.

Lack of monitoring has resulted in inaccuracies in the program's database, as well as use of the program by businesses without proper certification through OMWBE. Program officials cite lack of resources and the need for program simplicity to increase participation as the reasons for weak program controls. Finally, we did not find evidence to show that the program unnecessarily duplicates other public or private efforts.

Program Results and Effectiveness

The program does not have performance indicators and supporting data. Performance information is largely anecdotal, which includes participants'

views on the program's usefulness. Both loan recipients and banks commented favorably on the program.

Continuing Program Need

Program officials have presented qualitative information to demonstrate the need to continue the program. We did not find statistical evidence that identifies lack of access to capital by businesses owned by minorities and women in Washington.

Based on the comments received from Linked Deposit loan recipients and lenders, as well as our review of loan records, we can say that the program has made a positive difference for a number of its participants. If the program is continued, we recommend statutory as well as other modifications to address management controls and performance measures.

Recommendations

1. The legislature should consider putting a ceiling on the maximum amount that can be borrowed by a Linked Deposit loan applicant.
2. The Office of the State Treasurer, CTED, and OMWBE should develop and implement limited procedures for monitoring the Linked Deposit Program. This should include the following:
 - (a) Obtain from participating banks information such as minority and women's business enterprise certification status, loan amount, interest rate, loan term, purpose of the loan, and business name and address for each Linked Deposit loan recipient before the State Treasurer purchases certificates of deposit for such loans.
 - (b) Ensure that non-certified minority and women's business enterprises do not obtain or maintain the reduced interest rate loans under the program.
3. CTED and OMWBE should establish modest, cost-effective, yet meaningful, indicators to measure program performance.
4. In the absence of sufficient statistical evidence demonstrating the program's continuing need, the legislature should consider modifications discussed in Recommendations 1 through 3 if it decides to continue the Linked Deposit Program.